

UNEMPLOYMENT INSURANCE TAX

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Unemployment Insurance (UI) is a federal-state program jointly financed through Federal and state employer payroll taxes (federal/state UI tax). Generally, employers must pay both state and Federal unemployment taxes if:

1. they pay wages to employees totaling \$1,500, or more, in any quarter of a calendar year; or
2. they had at least one employee during any day of a week during 20 weeks in a calendar year, regardless of whether or not the weeks were consecutive. However, some state laws differ from the Federal law and employers should contact their state workforce agencies to learn the exact requirements. [Click here for state links.](#)

FEDERAL UNEMPLOYMENT TAX ACT

The Federal Unemployment Tax Act (FUTA), authorizes the Internal Revenue Service (IRS) to collect a Federal employer tax used to fund state workforce agencies. Employers pay this tax annually by filing IRS Form 940. FUTA covers the costs of administering the UI and Job Service programs in all states. In addition, FUTA pays one-half of the cost of extended unemployment benefits (during periods of high unemployment) and provides for a fund from which states may borrow, if necessary, to pay benefits. See IRS forms [940](#) and [940 Schedule A](#) for FUTA year 2012 Federal Unemployment Taxes.

FEDERAL TAX RATE

FUTA taxes are calculated by multiplying 6.0 percent times the employer's taxable wages. The taxable wage base is the first \$7,000 paid in wages to each employee during a calendar year. Employers who pay their state unemployment taxes on a timely basis receive an offset credit of up to 5.4 percent regardless of the rate of tax paid to the state. The FUTA tax rate for employers in states not subject to a FUTA credit reduction is generally 0.6% (6.0% - 5.4%), for a maximum FUTA tax of \$42.00 per employee, per year ($0.006 \times \$7,000 = \42.00).

STATE UNEMPLOYMENT TAX

State law determines individual state unemployment insurance tax rates. See the table of [current tax rates and taxable wage base information for individual states](#). The state unemployment tax, paid to state workforce agencies, is used solely for the payment of benefits to eligible unemployed workers.

WORKER MISCLASSIFICATION

Worker misclassification occurs when an employer incorrectly classifies a worker as a non-employee. Consequently, employers do not remit the appropriate amount of Federal and state employment taxes, and workers may not receive unemployment insurance benefits or the appropriate protections afforded to them as employees under the Fair Labor Standards Act, Occupational Safety and Health Act, and other Federal laws directed toward the protection of workers. Misclassifications can result from erroneous interpretation of the rules or from intentional disregard of the law. Interested parties may obtain [information about the UI employer-employee relationship tests used in a state](#) and a [directory of UI Tax offices](#). This information is published annually by the Office of Unemployment Insurance.

The rules that determine classification for employment at the Federal level follow common law. For IRS, the facts that provide evidence of the degree of control and independence fall into three categories:

- ▶ **Behavioral:** Does the company control or have the right to control what the worker does and how the worker does his or her job?
- ▶ **Financial:** Are the business aspects of the worker's job controlled by the payer?
- ▶ **Type of Relationship:** Are there written contracts or employee type benefits, such as pension plan, insurance, vacation pay, etc.? Will the relationship continue and is the work performed a key aspect of the business?

These factors are evaluated on [IRS Form SS-8](#), which employers and workers can file with the IRS to request a determination of the status of a worker for purposes of Federal employment taxes and income tax withholding. State unemployment insurance agencies use their own rules to determine whether to categorize an activity as employment for state UI purposes

DOMESTIC EMPLOYERS COVERAGE

Generally, employers of domestic employees must pay state and Federal unemployment taxes if they pay cash wages to household workers totaling \$1,000, or more, in any calendar quarter of the current or preceding year. A household worker is an employee who performs domestic services in a private home. Examples of household employees are: babysitters, caretakers, cleaning people, drivers, nannies, health aides, yard workers and private nurses.

EMPLOYERS OF AGRICULTURAL EMPLOYEES

Generally, employers of agricultural employees must pay state and Federal unemployment taxes if they pay wages to employees of \$20,000, or more, in any calendar quarter; or employ 10 or more workers in each of 20 different calendar weeks in the current or preceding calendar year. The 20 weeks do not have to be consecutive weeks, nor must they be the same 10 employees, nor must all employees be working at the same time of the day.